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UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF CALIFORNIA

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EASTERN DISTRICT OF CALIFORNIA

SACRAMENTO DIVISION

In re FOSTER and TERESA BROOKS, Debtors.	Case No. 08-31810-A-13G Docket Control No. SBS-1 Date: May 4, 2009 Time: 9:00 a.m.

MEMORANDUM

This Memorandum supplements the court's ruling appended to the minutes of the May 4 hearing[1] on the motion to confirm the first amended plan.

Creditor Scott Brooks was the sole objector to confirmation of the first amended plan. He believes that the debtors have not

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[1] The minutes, item 165 on the docket, erroneously state that they are for the hearing on April 6. Also, the ruling appended to the minutes addresses the first amended plan without the further amendment made at the May 4 hearing. Originally, the first amended plan provided for a 100% dividend to Class 7 nonpriority unsecured creditors, plus interest. This was changed at the hearing (as indicated in the confirmation order). Instead, Class 7 unsecured creditors will receive a dividend only if the debtors recover on their claim against Scott Brooks. In the event of a recovery, nonpriority unsecured creditors will receive as much as payment in full plus interest at the federal judgment rate. If there is no recovery, these creditors will be paid nothing.

proven that the plan is feasible. See 11 U.S.C. § 1325(a)(6).

As the plan was further amended at the May 4 confirmation hearing, unsecured creditors will not be paid a dividend unless the debtors are successful in the pending state court litigation against Scott Brooks. In that event, unsecured creditors will receive any recovery up to the full amount of their claims, plus interest at the federal judgment rate.

It was conceded at the confirmation hearing that absent a viable claim against Scott Brooks, unsecured creditors would not be entitled to a dividend. That is, if this case were proceeding under chapter 7, absent a litigation victory against Scott Brooks, there would be no nonexempt assets to fund the payment of the claims of nonpriority unsecured creditors. See 11 U.S.C. § 1325(a)(4). Therefore, in order to satisfy section 1325(a)(4), the proposed plan need only promise to pay unsecured creditors whatever is recovered in the litigation.

The state court litigation parallels a dischargeability complaint, Adv. No. 08-2685, filed by Scott Brooks. This court earlier modified the automatic stay to permit all parties to litigate their claims against one another in state court, and it stayed the adversary proceeding pending completion of the state court litigation.

A victory by Scott Brooks in state court will have two likely consequences for the debtors' chapter 13 case. First, there will be nothing to pay to unsecured creditors. Second, this court must next determine whether the state court judgment is a nondischargeable obligation of the debtors.

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On the other hand, if the debtors prevail against Scott Brooks, two other consequences are likely to follow. First, Scott Brooks will not have a claim against the debtors. Second, unsecured creditors will be paid from any recovery against Scott Brooks.

Hence, whatever the result of the state court litigation, Scott Brooks is unlikely to receive a dividend in this chapter 13 case.

This possible result squares with the confirmation requirements imposed by sections 1322(a) and 1325(a). See 11 U.S.C. §§ 1322(a) & 1325(a).

As to feasibility (see 11 U.S.C. § 1325(a)(6)), the debtors need not prove that they are likely to prevail in state court against Scott Brooks. Their plan does not depend on any such recovery to fund the payment in full of priority claims (see 11 U.S.C. § 1322(a)(2)) or secured claims (see 11 U.S.C. § 1325(a)(5)(B)). These dividends will be paid from income sources other than a litigation recovery. No challenge was raised to the dependability of these other income sources.

And, because it was conceded at the confirmation hearing that unsecured creditors would receive no dividend if this case proceeded under chapter 7 absent a recovery by the debtors against Scott Brooks, satisfying section 1325(a)(4) requires only that the plan provide for the payment of any recovery to nonpriority unsecured creditors. The debtors do not have to prove they can fund a "best-interests-of-creditors" dividend because none is required absent a litigation recovery.

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Thus, even if the debtors had no claim against Scott Brooks, their plan could be confirmed. Their regular income funds all necessary dividends payable to priority and secured creditors, and nonpriority unsecured creditors would be entitled to nothing.

Put differently, if this court concluded that the debtors' claim against Scott Brooks had no value, or that the debtors had no chance of success, the plan could still be confirmed. Without that claim, unsecured creditors would receive nothing in a chapter 7 case and therefore section 1325(a)(4) does not require any dividend in a chapter 13 case.

Dated: 2 June 2009

By the Court

Michael S. McManus, Judge
United States Bankruptcy Court

CERTIFICATE OF MAILING

I, Susan C. Cox, in the performance of my duties as a judicial assistant to the Honorable Michael S. McManus, mailed by ordinary mail to each of the parties named below a true copy of the attached document.

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Dated: June 2, 2009

Susan C. Cox

Susan C. Cox
Judicial Assistant to Judge McManus